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No. 89-95

In the Supreme Court of the United States

OCTOBER TERM, 1989

RIVERFRONT ASSOCIATES, LTD., ET AL., PETITIONERS

v.

FEDERAL SAVINGS AND LOAN INSURANCE CORPORATION, AS RECEIVER FOR MAINLAND SAVINGS & LOAN ASSOCIATION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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QUESTION PRESENTED

Whether the court of appeals correctly held that petitioners, who borrowed money from a savings and loan association that was subsequently placed in a Federal Savings and Loan Insurance Corporation (FSLIC) receivership, were precluded by the doctrine of *D'Oench, Duhme & Co.* v. *FDIC*, 315 U.S. 447 (1942), from asserting against FSLIC certain defenses to repayment of their loan.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. A1-A4, A5-A9) is reported at 872 F.2d 955. The order of the district court (Pet. App. A10) is unreported.

JURISDICTION

The court of appeals entered its judgment on April 20, 1989. The petition for a writ of certiorari was filed on July 18, 1989. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. On August 28, 1984, petitioner Riverfront Associates, Ltd., borrowed $1.7 million from Mainland Savings Association to purchase real property for development purposes. Riverfront executed a note promising Mainland to repay that amount plus interest on or before March 31, 1985. At the same time, petitioners Talbot and Owen, together with GAF Structures, Inc.,[1] signed personal guarantees as security for payment of the note. The promissory note and the guarantees were unconditional and unqualified on their faces. No payment was ever made on the note.

In July 1985, Mainland commenced this action against petitioners and GAF in Oklahoma state court seeking payment under the note and guarantees. Petitioners and GAF raised several defenses against repayment. The defenses were based on the allegation that repayment was not required because Mainland had agreed, as part of the $1.7 million loan transaction, to lend Riverfront an additional $6.5 million for construction purposes but had breached that agreement. See Pet. App. A2.

On April 4, 1986, the Federal Home Loan Bank Board determined that Mainland was insolvent and appointed the Federal Savings and Loan Insurance Corporation (FSLIC) to be the receiver for the institution.[2] After removal of the case to the United

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[1] GAF, which was a defendant-appellee below, is not a petitioner in this case.

[2] Until August 9, 1989, FSLIC was the receiver for Mainland. On that date, the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Pub. L. No. 101-73, 103 Stat. 183, took effect. H.R. Conf. Rep. No. 222, 101st Cong., 1st Sess. (1989). Section 401(a)(1) of the Act abolishes FSLIC on the effective date of the Act. Section

States District Court for the Western District of Oklahoma, FSLIC moved for summary judgment on the ground that petitioners' defenses were barred by the doctrine of *D'Oench, Duhme & Co.* v. *FDIC*, 315 U.S. 447 (1942). The district court agreed. See Pet. App. A35. The court explained that, although certain of Mainland's records reflected a conditional approval by Mainland of a $6.5 million loan application (see *id.* at A40-A49), nothing in those documents indicated that Mainland had agreed to modify petitioners' payment obligations under the original note and guarantees. *Id.* at A19-A20, A26-A27.[3] Because the alleged additional-financing condition on repayment of the $1.7 million loan had neither been reduced to writing nor incorporated within the terms of the note, the court held that this was "a classic case for the application of the *D'Oench* doctrine" and that petitioners were accordingly precluded from asserting the alleged side agreement to defeat the FSLIC's interest in enforcing payment of the note and guarantees. Pet. App. A35.

2. The court of appeals affirmed. Pet. App. A1-A4, A5-A9. The court noted that, although the FSLIC is not within the scope of 12 U.S.C. 1823(e) (barring assertion of certain defenses against the Federal Deposit Insurance Corporation (FDIC)), the FSLIC is protected by the federal common law doctrine of *D'Oench, Duhme*, which "established that the

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401(f)(2), however, declares that suits by or against FSLIC shall not abate.

[3] The $6.5 million loan was not to be made to Riverfront—the borrower on the $1.7 million loan—but to an entity called Plaza Del Rio, Ltd. Petitioners and GAF were to be the guarantors on that loan. See Pet. App. A40, A48.

debtor's signing of a facially unqualified note subject to an unwritten and unrecorded condition constitutes an arrangement which is likely to mislead federal insurers in contravention of the policy to protect them in their evaluation of financial institutions." Pet. App. A2-A3. The court also quoted this Court's recent explanation of the policy underlying *D'Oench, Duhme*: " 'Neither the FDIC nor state banking authorities would be able to make reliable evaluations if bank records contained seemingly unqualified notes that are in fact subject to undisclosed conditions.' " *Id.* at A3 (quoting *Langley* v. *FDIC*, 108 S. Ct. 396, 401 (1987)). Observing that petitioners "[did] not contest the principles established in *D'Oench* and *Langley*" but only their application here (Pet. App. A4), the court concluded that, contrary to petitioners' contention, there was not in fact a written agreement in Mainland's records that modified the terms of the $1.7 million note. In particular, the court of appeals concluded: "Nothing in the note, accompanying security agreements or other documents pertaining to the transaction evidences any type of conditional promise or side agreement on the part of Mainland of which the FSLIC might have been aware." *Ibid.*

ARGUMENT

Petitioners challenge the court of appeals' ruling on essentially two grounds. First, they contend that the court of appeals erroneously extended 12 U.S.C. 1823(e) from the FDIC to the FSLIC. Second, petitioners contend that the *D'Oench, Duhme* doctrine should not have been applied to this case because loan commitment papers for a second loan were contained within Mainland's files. See Pet. I, 5-7.[4] Those arguments are without merit and do not warrant this Court's review.

1. Petitioners' first contention relies on an incorrect characterization of the court of appeals' ruling. Contrary to petitioners' suggestion (Pet. 5), the court of appeals did not base its decision on 12 U.S.C. 1823(e). Indeed, the court expressly recognized that the provision "by its terms applies only to the FDIC." Pet. App. A3. The court of appeals instead decided that petitioners' defenses were barred by the federal common law doctrine established by *D'Oench, Duhme*, which, as the court correctly noted, survives "as an independent basis for protecting the FSLIC from undisclosed agreements." *Ibid.* Accordingly, no question regarding the application of 12 U.S.C. 1823(e) to the FSLIC is presented by the decision below.

2. Petitioners' second contention challenges the court of appeals' holding that *D'Oench, Duhme* bars their defenses. Petitioners do not dispute that the

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[4] Petitioners also make a wholly unexplained suggestion (Pet. 7) that the Court grant certiorari to decide whether to "apply the same rationale" in this case as the rationale applied in *Coit Independence Joint Venture* v. *FSLIC*, 109 S. Ct. 1361 (1989), a case that did not involve *D'Oench, Duhme* or 12 U.S.C. 1823(e).

D'Oench, Duhme doctrine applies to the FSLIC.[5] They challenge only the court of appeals' application of the doctrine to the facts of this case. That fact-specific challenge is meritless, because the court's application of *D'Oench, Duhme* in this case was correct.

As this Court explained in *Langley*, 108 S. Ct. at 402, the *D'Oench, Duhme* doctrine bars a borrower's assertion of a defense based on an arrangement with a financial institution that would "tend to deceive" or be "likely to mislead" the regulatory authorities. Furthermore, "one who signs a facially unqualified note subject to an unwritten and unrecorded condition upon its repayment has lent himself to" just such an arrangement, "whether the condition consists of performance of a counterpromise (as in *D'Oench, Duhme*) or of the truthfulness of a warranted fact." *Ibid.* See *D'Oench, Duhme*, 315 U.S. at 456-462. This case falls squarely under those principles. Petitioners signed facially unqualified notes and guarantees; their defenses rest on the allegation that Mainland agreed to provide additional funding and that provision of such funding was a condition of repayment of the original $1.7 million loan. But, as the district court (Pet. App. A19-A20, A26-A27) and the court of appeals (*id.* at A4) both concluded, that alleged condition was not part of any agreement with Mainland that the FSLIC might have been aware of. In particular, although Mainland's loan

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[5] The courts have uniformly held the *D'Oench, Duhme* doctrine applicable to the FSLIC. See *Firstsouth, F.A.* v. *Aqua Const., Inc.*, 858 F.2d 441, 442-443 (8th Cir. 1988); *FSLIC* v. *Lafayette Inv. Prop., Inc.*, 855 F.2d 196, 198 (5th Cir. 1988); *Taylor Trust* v. *Security Trust Fed. S&L Ass'n*, 844 F.2d 337, 342 (6th Cir. 1988).

committee did, as petitioners state, give conditional approval to a $6.5 million loan to be made to one of petitioners' entities,[6] nothing in the approval documents contains any written agreement on the part of Mainland to modify petitioners' unconditional obligations under the $1.7 million note.[7] In these circumstances, petitioners are barred by *D'Oench, Duhme* from seeking to avoid their obligation to repay the $1.7 million they borrowed from Mainland.[8]

In any event, the question of *D'Oench, Duhme*'s scope as applied here is of little if any continuing importance. Under the recently enacted Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Pub. L. No. 101-73 (Aug. 9, 1989), not only was the FSLIC abolished (§ 401(a)(1)), but all newly created federal-agency receiverships of federally insured depository institutions, as well as certain recently created receiverships, are covered by

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[6] The approval in question was subject to a number of conditions that petitioners have not shown they ever satisfied. See Pet. App. A48-A49. Petitioners and Mainland never actually entered into a loan agreement based on that approval.

[7] Petitioners' application for the original $1.7 million loan has an attachment providing that the loan "will be rolled into" subsequent financing. Pet. App. A42. Whatever the precise meaning of that attachment, however, the application was not a binding commitment. The application states: "this application shall not be construed as a commitment. Mainland Savings shall not be bound by any of the terms and conditions of this application." *Id.* at A41. Rollover financing was not made a condition of the $1.7 million note and guarantees signed by petitioners.

[8] The *D'Oench, Duhme* doctrine equally bars petitioners from relying on the alleged side agreement to obtain damages to offset their repayment obligation. See *Beighley* v. *FDIC*, 676 F. Supp. 130, 132 (N.D. Tex. 1987), aff'd, 868 F.2d 776 (5th Cir. 1989).

the newly amended version of the statutory counterpart to *D'Oench, Duhme*, 12 U.S.C. 1823(e).[3] That provision greatly reduces the number of occasions on which reference to *D'Oench, Duhme* would be necessary. Moreover, for pre-Act receiverships like the one in the present case, even aside from the possible applicability of 12 U.S.C. 1823(e) itself to the FDIC as successor receiver, the Act lends support to the court of appeals' application of *D'Oench, Duhme* to bar petitioners' defenses: the Act's extension of Section 1823(e) reaffirms *D'Oench, Duhme*'s policy of ensuring that federal regulators can rely on the written terms of financial institutions' assets.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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SEPTEMBER 1989

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[3] Section 217 of the new Act amends 12 U.S.C. 1823(e) to make it expressly applicable to notes acquired by the FDIC as receiver. That provision is applicable to the Resolution Trust Corporation, which, among other duties, serves as successor receiver in cases where the FSLIC was appointed receiver on or after January 1, 1989. § 501(a) (to be codified at 12 U.S.C. 1441a(b)(4)). Newly created federal receiverships have either the FDIC or the Resolution Trust Corporation as receiver. § 501(a) (to be codified at 12 U.S.C. 1441a(b)(4) and (6)); § 212(a) (to be codified at 12 U.S.C. 1821(c)).

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